**Before the**
**FEDERAL COMMUNICATIONS COMMISSION**
**Washington, D.C. 20554**

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| In the Matter of the | ) | |
| The Federal-State Joint Board | ) | |
| On Universal Service | ) | CC Docket No. 96-45 |
| | ) | |

**COMMENTS OF SUREWEST COMMUNICATIONS**
**ON RECOMMENDED DECISION**

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## SUMMARY

In these Comments, SureWest Communications demonstrates that the proposals in the Recommended Decision (hereinafter "*RD*") do not fulfill the requirements of Section 254 of the Communications Act to ensure comparable and affordable rates, do not fulfill the mandates of the Tenth Circuit remand, and are otherwise flawed and arbitrary policies. Furthermore, the *RD* does not appropriately address the needs of mid-sized incumbent local exchange carriers ("ILECs") such as SureWest's subsidiary Roseville Telephone Company ("RTC") which have been classified as "non-rural" for purposes of federal high-cost support, but which in fact are exponentially smaller than the huge Bell Operating Companies with which they are included. The result of this inappropriate classification has been the loss of federal high-cost support to subscribers in a high-cost area.

First, as ably demonstrated in the Separate Statements of Commissioner Martin and Commissioner Rowe, the use of state-wide averaged costs of providing service to determine eligibility for federal high-cost support fails to meet the Section 254 mandate for comparison of rates. The *RD*'s proposed "supplemental" rate-based analysis to be performed by each state as part of a certification is no solution because it fails to actually compare rates. The mere fact that all rates in a state are under some set benchmark does not, as a matter of logic or fact, mean that all of the rates under that benchmark are comparable. Due to differences in economies of scale, and the ability of RTC's surrounding provider SBC to average rates on a state-wide basis including major urban centers, RTC's basic residential local service rates are 85% higher than

SBC's California basic rates. Yet, while RTC's rates clearly are not comparable with SBC's rates, under the policies in the *RD*, RTC would not receive any federal universal service support, even though the State of California can certify that both rates are under the "benchmark".

The *RD*'s continued use state-wide averaged costs based on the Commission's forward looking cost proxy model, rather than looking at actual rates, to determine high-cost support, is a deeply flawed policy. First, the use of the proxy model is not appropriate for carriers, such as RTC, that lack the economies of scale and scope of BOCs. Use of the proxy cost model is similarly inappropriate for carriers like RTC which have only two wire centers (as opposed to the thousands of wire centers that each of the BOCs have), since there is little chance for discrepancies between the proxy and real costs to average out. This issue was recognized by discussed by the Rural Task Force.

The use of the 135 percent benchmark is also flawed, since regardless of the statistical justifications in the *RD*, the bottom line on the effect of using the 135 percent figure is that federal funding is denied to almost all states. As Commissioner Rowe noted, some states receive no support, even though their costs are not reasonably comparable, and nothing in the legislative history of the 1996 Telecommunications Act suggests that Congress intended universal service support to be available only to carriers or states in the top three percentiles of cost, the result of the standard deviation analysis in the *RD*.

In order to meet the comparability goals and mandate of the Act, RTC proposes that universal service must fund the difference between the current actual rates of a LEC and those of other LEC(s) in the same local market area. Accordingly, the FCC must establish a national policy for the rate comparability occurring within each state. RTC recommends a 120% factor be used for comparability of rates, though RTC recognizes that a factor of less than the 120% may also be a reasonable level for the application of federal high-cost support. This "Proper Zone of Reasonableness" ("PZOP") would provide the appropriate mechanism for a comparability factor for the local market area. Further, since universal service is an obligation that is shared between federal and state support mechanisms, a similar or higher rate comparison benchmark should be established by each state for the state's provision of its universal service support. The difference between the state rate benchmark and the 120 percent national benchmark would be funded through federal universal service.

In sum, the FCC should modify the current "non-rural" federal support mechanism as proposed herein, to make it consistent with the Act and appropriate for application to all carriers. In addition, the FCC should revise the definition of "non-rural" carrier to exclude carriers such as RTC.

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**COMMENTS OF SUREWEST COMMUNICATIONS**
**ON RECOMMENDED DECISION**

SureWest Communications, by its attorney, hereby responds to the *Public Notice,* DA 02-2976, released November 5, 2002, seeking comments on the Recommended Decision issued by the Federal-State Joint Board on Universal Service on October 16, 2002 (FCC 02J-2, hereinafter "*RD*"). As discussed further below, SureWest asserts that the proposals in the *RD* do not fulfill the requirements of Section 254 of the Communications Act to ensure comparable and affordable rates, do not fulfill the mandates of the Tenth Circuit remand, and are otherwise flawed and arbitrary policies. Furthermore, the *RD* does not appropriately address the needs of mid-sized incumbent local exchange carriers ("ILECs") which have been classified as "non-rural" for purposes of federal high-cost support, but which in fact are exponentially smaller than the huge Bell Operating Companies with which they are included. In addressing the flaws in the *RD*, the FCC should modify the current "non-rural" federal support mechanism as proposed herein, to make it consistent with the Act and appropriate for application to all carriers. In addition, the FCC should revise the definition of "non-rural" carrier to exclude carriers such as RTC.

## I. Introduction

SureWest is a facilities-based provider of telecommunications services, based in Northern California. Through its subsidiary companies, SureWest provides incumbent local exchange, competitive local exchange, directory advertising, long distance, cable television, broadband and PCS services. SureWest's subsidiary Roseville Telephone Company ("RTC") is an ILEC serving subscribers in south Placer and northern Sacramento counties.

RTC currently serves approximately 137,000 access lines.[1] This figure places RTC a mere 37,000 access lines above the definition of a "rural" telephone company. It is by far the smallest of the "non-rural" LECs with which RTC has been co-classified for purposes of federal high-cost support. In comparison, the two largest LECs, SBC and Verizon (who both provide ILEC service in California), have approximately 59,500,000 and 61,600,000 access lines, respectively.[2] Verizon thus has approximately 450 times as many access lines as RTC. Similarly, while these LECs have thousands of central offices,[3] RTC has only two: located in the towns of Roseville and Citrus Heights.

In sum, RTC is exponentially smaller than these two LECs serving California, and as a result it lacks the economies of scale and scope of such carriers. For various

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1 RTC's Study Area covers 131,839 "subscriber loops", as set forth in the USAC Fourth Quarter 2002 Administrative Filing, Appendix HC04. The difference between the number of "access lines" and the number of "subscriber loops" is that several services are not included in the count of "subscriber loops", including remote call forwarding, special access and WATS.

2 As reported in USTA's Phone Facts 2003.

3 In research last year, RTC concluded that Verizon had over 6,200 wire centers, while SBC had over 3,200 wire centers.

reasons, including the fact that RTC lacks these economies of scale and scope, RTC is in fact a high cost carrier. Consistent with that fact, RTC previously received approximately $1.7 million per year in support under the previous federal high-cost support regulatory regime.[4] That support was phased out when the Commission enacted its forward looking cost-based regulations in the Ninth Report and Order in CC Docket 96-45, and used the definition of "rural telephone company" in Section 3(37) of the Communications Act (essentially, more than100,000 access lines in a study area) as the criterion of eligibility for federal support in the Tenth Report and Order. The result of losing that support substantially shifts the responsibility for recovering these revenue requirements onto RTC's local rate payers. The only remaining source for recovering these costs is to increase already high basic service rates.

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[4] While $1.7 million may not sound like a large amount of money for some carriers, it is for RTC. Furthermore, the RTC study area serves less than 200,000 lines, and under the prior federal high-cost support regulations, study areas below this level received significantly more support than those with more than 200,000 lines. As a result, RTC has had a significantly higher reliance on federal support than other "non-rural" carriers, as shown in the table below, of figures obtained from the USAC Quarterly Administrative Filing, 1Q01:

Table 1

| | **Company** | **USF as % of Loop Revenue Requirement** |
|---|---|---|
| 1 | Verizon | 0.539% |
| 2 | Verizon (w/o PR) | 0.188% |
| 3 | SBC | 0.027% |
| 4 | BellSouth | 0.183% |
| 5 | Qwest | 0.294% |
| 6 | RTC[1] | **6.682%** |

RTC filed a petition for reconsideration of that portion of the Tenth Report & Order that used the 100,000 access line definition of "rural telephone company" as the dividing line between different high-cost support mechanisms for "rural" and "non-rural" LECs.[5] RTC noted that Section 254 of the Communications Act does not require use of that definition, and that its use improperly places smaller mid-sized carriers in the same category as LECs hundreds of times their size, thus basing high-cost support for such companies on models designed for carriers with substantially greater economies of scale and scope. In addition, RTC noted that the loss of federal support resulting from use of that definition will put substantial pressure on the local rates of carriers such as RTC. RTC thus urged the Commission to revise that definition in a manner that treats the smaller mid-sized carriers in a manner more similar to the rural LECs.[6] RTC suggested that such a revision should either rely on the "two percent" definition of "rural carrier" in Section 251(f)(2) of the Communications Act, or should distinguish "non-rural"

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[5] In hindsight, the use of the terms "rural" and "non-rural" in the context of universal service reform, is unfortunate. Such terms create incorrect implications regarding the size and cost structure of a company based on the location of the company's service area. In addition, "non-rural" companies serve the majority of the rural areas, while some "rural" companies serve in urban areas.

[6] It should be noted that certain mid-sized ILECs such as Alltel (2.6 million total access lines according to Phone Facts 2003), Citizens Communications (2.5 million total access lines), CenturyTel (1.8 million total access lines) and TDS (650,000 total access lines) are significantly larger than RTC. Yet, those larger companies are classified as "rural" and accordingly receive federal support, largely through their use of multiple subsidiaries with separate study areas, each of which is under the 100,000 access line threshold. By comparison, RTC has not created subsidiary companies with multiple study areas. The arbitrariness of the current definition of "non-rural" federal support mechanism is demonstrated by the fact that these substantially larger companies receive federal support, while RTC does not.

LECs as those with more than 200,000 access lines in a study area. The Commission has never addressed RTC's Petition.[7]

Subsequent *Recommended Decisions* of the Joint Board have continued to rely on the flawed use of the 100,000 access line distinction between carriers subject to "rural" and "non-rural" treatment for federal high cost support. As shown below, regardless of the impact on truly large carriers, the proposals in the current *RD* fail to meet the requirements of Section 254 of the Act to ensure comparable and affordable rates, and the proposals are inappropriate as applied to a carrier like RTC. Accordingly, the *RD* is fatally flawed.

## II. The Policies in the *RD* Do Not Fulfill the Requirements of Section 254 or the Court Remand, and are Otherwise Flawed.

While SureWest recognizes that the Joint Board put a lot of work into the *RD*, unfortunately the result is a flawed reaffirmation of the very policies called into question and remanded by the Tenth Circuit in the *Qwest* decision. These policies fail to fulfill the provisions of Section 254 that require support for high-cost areas, and that require comparable rates. Furthermore, the *RD* is also flawed because the policies stated therein are not appropriate for a carrier such as RTC.

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[7] While the Tenth Circuit Court of Appeals upheld the Tenth Report and Order, it never addressed the issue in RTC's Petition, *i.e.* the arbitrary use of the 100,000 access line definition of "rural telephone company" as the dividing line between different high-cost support mechanisms or "rural" and "non-rural" LECs. Qwest Corp. v. FCC, 258 F.3d 1191 (2001) (hereinafter "*Qwest*").

A. The *RD* Does Not Fulfill the Section 254 Requirement For Comparability of Rates, and for Support of All High-Cost Areas.

Section 254(b)(3) sets out, as a principle for federal universal service support, the requirement that consumers "in rural, insular and high cost areas, should have access to [telecommunications services] that are reasonably comparable to those provided in urban areas and that are available at rates that are reasonably comparable to rates charged for similar services in urban areas." The *RD* fails to fulfill these requirements.

First, the *RD* again supports the use of state-wide averaged costs of providing service to determine eligibility for federal high-cost support that is supposed to be based on comparability of rates. As ably demonstrated in the Separate Statements of Commissioner Martin and Commissioner Rowe, however, there are numerous flaws in such an approach. As Commissioner Martin stated, "I am not convinced that a mechanism based solely on costs would meet the statutory mandate requiring a comparison of rates."[8] In fact, such a mechanism cannot meet that statutory mandate.

In paragraph 19, the *RD* attempts to justify this approach by suggesting that states have greatly varied rate design policies, and that as a result, any comparison of rates could lead to inequitable treatment between carriers in different states with similar costs but different local rate design policies. The Joint Board is suggesting that a rate-based analysis is either too difficult and burdensome, or that it is impossible. There is

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[8] Separate Statement of Commissioner Kevin Martin at page 2. *See also* Separate Statement of Commissioner Bob Rowe, at pages 1-14.

no evidence that such an analysis is impossible, and while it may be difficult to create a mechanism that takes into account differing state policies, such difficulty provides no basis for ignoring a statutory mandate. Indeed, given that Section 254 explicitly refers to comparable rates, if Congress had wanted to determine eligibility for federal universal service support based on costs, it would have included this language in the statute. However, it did not do so and specifically required that the Commission focus on rural, insular and high cost areas having rates that are reasonably comparable to rates charged for similar services in urban areas. The *RD* provides no valid justification for ignoring this statutory mandate.

Further evidence of the weakness of the *RD*'s explanation for use of a primarily cost-based analysis is the fact that it nevertheless added a "supplemental" rate-based analysis to be performed by each state as part of a certification.[9] Yet even this mechanism fails to actually compare rates. The mere fact that all rates in a state are under some set benchmark does not, as a matter of logic or fact, mean that all of the rates under that benchmark are comparable. The hypothetical rates of $10 per month and $29 per month are both below the benchmark of $30.16, but would anyone reasonably believe those two rates to be comparable? The answer is obviously, no. In a recent proceeding, even the California Public Utilities Commission Office of Ratepayer

[9] As noted by Commissioner Martin, if the Joint Board felt confident that the primary cost-based analysis fulfilled the requirement for comparison of rates, then why did it add the "supplemental" rate analysis? Separate Statement at page 2. Similarly, if the Board is concerned about the difficulty of comparing rates, why does it think that comparing costs and rates will be easier?

Advocates stated that if one assumes a mandate that rates between carriers be comparable and that subscribers in one company were paying twice as much for the same service as provided by another carrier, then the subscribers <u>would not</u> be paying comparable rates.[10]

SureWest is equally concerned about the failure of the *RD* to effectively fulfill the requirement in Section 254 that high-cost areas have rates comparable to low-cost areas. Commissioner Rowe notes that if the *RD* is adopted by the FCC, "some 'non-rural' carriers (more properly, large companies serving high cost areas) would not receive sufficient support...." Separate Statement at page 1. This statement points out one way in which the *RD* fails to fulfill the Section 254 obligation regarding high-cost areas: that carriers, such as RTC, have been improperly categorized as "nonrural" and that as a result, will be improperly denied support that is allocated to "rural" carriers. Adopting the RD would in fact make this true. As shown in Table 2 following, RTC currently has basic residential local service rates that are 85% above SBC's California basic residential local service rates. RTC's current business local rates are 139% above SBC's California business local rates.

[10] Investigation 01-04-026. Reporters Transcript, Vol 4, p. 263:8-20.

| | | | | |
|---|---|---|---|---|
| | **TABLE 2** | | | |
| | **Basic Rate Comparison of RTC to SBC-California** | | | |
| | | | | |
| | **Residence** | RTC | SBC | RTC Rates Compared to SBC |
| 1 | Basic Rate - Flat rated | $ 18.90 | $ 10.69 | 177% |
| 2 | End User Common Line (EUCL) Charge | $ 6.00 | $ 4.48 | 134% |
| 3 | Residence-Initial Minute | $ 0.0808 | $ 0.0676 | 120% |
| 4 | Residence-Additional Minute | $ 0.0350 | $ 0.0151 | 232% |
| 5 | Surcharge Additive | 8.43% | -1.30% | 851% |
| | | | | |
| 6 | Average Monthly Basic Service Rate | **$31.24** | **$16.90** | 185% |
| | | | | |
| | **Business** | RTC | SBC | |
| 1 | Basic Rate - Measured | $ 25.90 | $ 9.80 | 264% |
| 2 | End User Common Line (EUCL) Charge | $ 9.20 | $ 4.48 | 205% |
| 3 | Business-Initial Minute | $ 0.0450 | $ 0.0279 | 161% |
| 4 | Business-Additional Minute | $ 0.0150 | $ 0.0088 | 170% |
| 5 | Business Extended Area-Initial Minute | $ 0.0808 | $ 0.0676 | 120% |
| 6 | Business Extended Area-Additional Minute | $ 0.0350 | $ 0.0151 | 232% |
| 7 | Surcharge Additive | 8.43% | -1.30% | 851% |
| | | | | |
| 8 | Average Monthly Basic Service Rate | **$57.20** | **$23.94** | 239% |

Accordingly, RTC's rates are not comparable with SBC's California urban rates and under the *RD*, RTC would not receive any federal universal service support. This is a core flaw in the entire federal support system, because it results in study areas not receiving support that should under the comparability requirement. This flaw constitutes a failure to fulfill Section 254.

A second way in which the *RD* fails to fulfill the high-cost requirement is by its flawed definition of a "high-cost area": wire centers with less than 540 lines per square mile. *RD* at para. 50. In a manner similar to the flawed decision to use costs as a proxy for rates, the Board now proposes using line density as a proxy for determining which rural, insular and high cost areas to compare with urban areas. However, Section 254 requires comparability of rates for <u>all</u> rural, insular and high cost areas, not just those with a line density less than 540 lines per square mile. The *RD* approach would irrationally leave the study areas of RTC and other companies out of this comparison and certification process. RTC rates could be increased to any rate, for example $35 or even $75, and those rates would never be reviewed to determine conformance with the comparability provisions of Section 254. As a result, RTC subscribers are improperly excluded from the comparison required in the Act, and denied the opportunity to receive federal universal service funds supporting their high cost of service. The FCC should not allow such improper discrimination between companies, subscribers or areas of the nation in the provision of federal support.

In sum, the proposals in the *RD* fail to fulfill the requirement under Section 254 that federal support ensure that subscribers in high-cost areas have rates comparable to those in other areas. Accordingly, the *RD* improperly discriminates against RTC's subscribers and is arbitrary and capricious. While this alone is reason for rejecting the *RD* and taking up the task of creating a mechanism that fulfills the statutory mandate, there are numerous other reasons why the *RD* is flawed and must be rejected.

### B. Determining Federal Support Through Use of State-Wide Averaged <u>Costs, Rather Than Actual Rates, is an Arbitrary and Flawed Policy.</u>

The *RD*'s continued use of the Commission's forward looking cost proxy model as the basis for determining high-cost support is a deeply flawed policy. Reliance on such a model for calculating high-cost support is not in conformance with the mandate of the Act and is probably inappropriate as applied to all carriers, but it is certainly inappropriate as applied to RTC.

First, the use of the proxy model is not appropriate for carriers, such as RTC, that lack the economies of scale and scope of BOCs. The Joint Board and the Commission have acknowledged this very principle in the *RD*. *See, e.g.,* paragraph 28 where the Joint Board states “[w]hile statewide averaging is appropriate for the high-cost mechanism providing support to non-rural carriers, it may not be appropriate for the high-cost mechanism providing support to rural carriers. [citation omitted] Many rural carriers lack the economies of scale and scope of the generally larger non-rural carriers.”[11] Nevertheless, the Commission continues to apply this mechanism to RTC, a carrier which lacks these economies of scale and scope. It is flatly arbitrary, discriminatory and unjust for the Commission to base the calculation of federal support for carriers such as RTC on a mechanism that the Board itself admits is inappropriate in such a case.

In addition to being inappropriate for carriers such as RTC due to lack of economies of scope and scale, use of the proxy cost model is similarly inappropriate for carriers like RTC which have only two wire centers, since there is little chance for discrepancies between the proxy and real costs to average out. This issue was

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[11] *See also RD* at note 34 stating that because rural carriers have higher operating and equipment costs, due in part to a lack of economies of scale, the Commission has previously recognized that a separate approach was needed to determine support for rural carriers, and thus the Rural Task Force was established. Consistent with that analysis, the Rural Task Force Recommendation specifically lists differing economies of scale and scope as significant reasons why the FCC’s forward-looking proxy model is not appropriate for rural carriers. *See* Rural Task Force Recommendation to the Federal-State Joint Board on Universal Service, at page 12.

discussed by the Rural Task Force in its September 29, 2000 Recommendation to the Federal-State Joint Board on Universal Service. Therein, the RTF finds:

> "The aggregate results of this study suggest that, when viewed on an individual rural wire center or individual Rural Carrier basis, the costs generated by the Synthesis Model are likely to vary widely from reasonable estimates of forward-looking costs."[12]

In its White Paper 4, the RTF provides additional insight into why it reached its conclusion regarding the applicability of the model:

> "The 'Law of Large Numbers' suggests that for the RBOCs those wire centers where the support results are too high will tend to offset those which are too low, resulting in a reasonable result. This is not the case for many Rural Carriers who serve only a few wire centers, or in some cases, a single wire center."[13]

This same logic is equally applicable to RTC, which has only two wire centers. Thus, while the large number of wire centers that BOCs have in a particular state may result in an averaging out of discrepancies between the proxy model and the real costs of all those wire centers, such averaging is unlikely in the case of a carrier like RTC, which has only two wire centers. Accordingly, it is not appropriate to use the cost proxy model to calculate federal support for RTC.

Use of the forward looking costs as the basis for determining high-cost support for RTC is also unwise because such "costs", as noted by Commissioner Martin, "have little, if any, nexus to the establishment of end-user retail rates ... [and result] in support being provided to some areas with low end user rates while certain areas that have high

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[12] Rural Task Force Recommendation to the Federal-State Joint Board on Universal Service, page 18.

[13] Rural Task Force White Paper 4, A Review of the FCC's Non-Rural Universal Service Fund Method and the Synthesis Model for Rural Companies, at page 7.

rates receive insufficient support." Separate Statement at page 5.[14] RTC's situation is a prime example of Commissioner Martin's critique: it has a high cost study area with resulting rates significantly higher than those of the surrounding SBC areas, but receives no federal high-cost support. Clearly this is not the intended result of a rational support policy.

In sum, because carriers like RTC lack the economies of scale and number of wire centers of typical "non-rural" LECs, and because proxy costs have no real nexus with end-user rates or the costs used by states to set local rates, the use of statewide averaged costs as affirmed in the *RD* is arbitrary, unjust, and does not meet the mandate of the Communications Act of comparable rates, especially as applied to carriers such as RTC.

C. Use of the 135 Percent Benchmark is a Flawed Policy.

The current "non-rural" federal high-cost support mechanism provides support for carriers in states where intrastate costs (as determined by the proxy model) exceed 135 percent of the national average cost per line for non-rural carriers. In the *Qwest* decision, the Tenth Circuit found that the Commission had failed to adequately explain how it arrived at this 135 percent figure, and how use of that figure would achieve the goals of Section 254 of the Act. The *RD* now adds reliance on a GAO Study, "cluster analysis" and use of standard deviation statistical techniques to justify and reaffirm the

[14] Commissioner Rowe similarly questions "the accuracy of the model." Separate Statement at page 13.

135 percent figure. Commissioner Rowe ably demonstrates the flaws in each of these attempted justifications. Separate Statement at pages 2-9. But the bottom line on the effect of using the 135 percent figure is that federal funding is denied to almost all states. As Commissioner Rowe noted, some states receive no support, even though their costs are not reasonably comparable. Separate Statement at page 2. What is more disturbing is that, as Commissioner Rowe points out, nothing in the legislative history of the 1996 Telecommunications Act suggests that Congress intended universal service support to be available only to carriers or states in the top three percentiles of cost as reflected in the results of the standard deviation analysis. Separate Statement at page 7. Thus, even if use of statewide average costs were appropriate to determine federal funding, RTC shares Commissioner Rowe's view that the135 percent benchmark is clearly arbitrary and inappropriate, since it fails to fulfill the statutory mandate to provide high-cost support and ensure reasonable comparability of rates.

It is interesting that the *RD* seems to recognize the weakness of the 135 percent figure in discussing BellSouth's proposed additional lower benchmark for use in providing support for carriers in states with average costs below the 135 percent benchmark. Although the *RD* states that "the use of a step function may have benefits and warrants further consideration", the Board declines to recommend such an approach at this time, supposedly out of the need to act expeditiously. *RD* at para. 42. While the Board proposes addressing the alternate benchmark in some future "comprehensive review" of the rural and non-rural mechanisms, this response is disingenuous, as the Board well knows that such a comprehensive review is years away, while companies and end-users are left to suffer the results of the current flawed system in the interim. This can only be described as arbitrary and capricious decision-making.

D. The State Certification Proposal in the *RD* Fails to Fulfill the Court's Mandate to Induce States to Address Egregious Intrastate Rate Discrepancies.

One issue remanded back to the Commission by the Tenth Circuit was the failure of the Ninth Report and Order to include some inducement for states to assist in implementing universal service policies. In response, the *RD* proposes a procedure under which States would be required to certify that all local rates in high-cost areas within the state are below $30.16. This is a fatally flawed proposal.

Even if the definition of "high-cost areas" were appropriate, the revised state certification proposal fails to adequately address the Tenth Circuit's mandate to insure that rates are comparable within the states. As Commissioner Martin notes, "there must be a requirement that states address [rate] discrepancies within their borders …. Yet this decision fails to require that such inequities between urban and rural rates be addressed." Separate Statement at page 3.

This problem is particularly troublesome in California, where RTC operates. RTC is surrounded by SBC, so the comparable rates for consumers will invariably be those of SBC. As already shown in the Table 2 *supra,* due to differences in rate averaging and economies of scale, RTC's residential local rates are 185 percent of those of SBC in the surrounding areas. Roseville's business local rates are 239 percent of those of SBC in the surrounding areas. One major problem is that SBC rates are averaged state-wide through very dense population centers, and then applied to the high cost areas of Northern California where both SBC and RTC provide service. Further, the California Public Utilities Commission has a proceeding underway that is reviewing RTC's continued need of $11.5 million in revenue that it currently receives from a state universal service fund on an interim basis. California Public Utilities Commission Office of Ratepayer Advocates has proposed that if the proceeding shows that RTC's needs the $11.5 million to cover telephone service operating costs, RTC should recover this revenue through increases in rates to customers. If this $11.5 million is collected through residential rates, these rates would have to increase by $10.24. This would make RTC's residential local rates 245% percent of those of SBC in the surrounding areas.

RTC residential and business rates are currently 85% and 135%, respectively, higher than those in comparable service areas. With the loss of federal high-cost support after the enactment of the Ninth Report and Order, the gap between rates paid by RTC subscribers and those comparable areas will continue to increase. RTC subscribers are aware of the rate differences, and regularly express concern to RTC about the affordability of RTC rates.[15]

## III. RTC's Proposal for Revision to the *RD*

As discussed previously, the Telecommunications Act of 1996 addressed the need to maintain comparability of rates paid by telephone subscribers. Specifically, Section 254(b)(3) provides that, "Consumers in all regions of the Nation, including low-

[15] In RTC customer surveys, the number one complaint is the rate differential with SBC.

income consumers and those in rural, insular, and high cost areas, should have access to telecommunications and information services, including interexchange services and advanced telecommunications and information services, that are reasonably comparable to those services provided in urban areas and that are available at rates that are reasonably comparable to rates charged for similar services in urban areas." This mandate has not been achieved in general or as applied to RTC, and therefore, the *RD* must be modified to meet this requirement. The simple fact overlooked in the *RD* is that actual comparison of rates is required. While the RD claims it may be difficult to create the appropriate mechanism to compare rates, ultimately, a plan must be developed that meets the requirements of the Act.

In order to meet the comparability goals and mandate of the Act, universal service must fund the difference between the current actual rates of a LEC and those of other LEC(s) in the same local market area. Further, universal service is an obligation that must be fulfilled in an integrated approach, as this obligation is shared jurisdictionally between federal and state support mechanisms. Accordingly, a national policy must be set that recognizes the delicate balance in providing predictable and sufficient federal and state universal service funding to conform to the Act's mandate. In this regard, RTC proposes that the FCC establish a national rate benchmark for the federal universal service fund support, with the states adjusting their own state universal service mechanisms to provide the remaining support to meet the Act's obligations.

This integrated approach should be based on comparison of rates for the provision of basic local services in the state. For some states, that may be a combination of factors depending on their specific circumstances and the rate design adopted for providing basic local services. In California, this rate used for comparison purposes would be comprised of a number of components that compose the provisioning of the basic local service. To illustrate that structure, Table 2 *supra* shows a comparison of Roseville's basis local service rates with SBC's in California for both residential and business subscribers. Obviously, the current rates for RTC and SBC are quite disparate when compared and therefore do not meet the fundamental requirement of the Act.

Accordingly, the FCC must establish a national policy for the rate comparability occurring within each state. RTC recommends a 120% factor be used for comparability of rates, though RTC recognizes that a factor of less than the 120% may also be a reasonable level for the application of federal high-cost support. RTC is confident this "Proper Zone of Reasonableness" ("PZOP") would provide the appropriate mechanism for a comparability factor for the local market area. Further, since universal service is an obligation that is shared between federal and state support mechanisms, a similar or higher rate comparison benchmark should be established by each state for that state's provision of its own universal service support. The difference between the state rate benchmark and the 120 percent national benchmark would be funded through federal universal service.

RTC asserts that the elements listed in this proposal would meet the requirements of the Act. Such an approach would enable the states to maintain reasonably comparable rates between LECs within their state, and would provide for specific, predictable and sufficient federal and state mechanism(s) that support the goals of preserving and advancing universal service.

## IV. Conclusion

For the reasons discussed above, the proposals in the *RD* do not fulfill the mandate in Section 254 of the Act to ensure that subscribers in high-cost areas receive service at rates reasonably comparable to those in other areas. In addition, the use of state-wide average costs and the 135 percent benchmark are flawed policies that do not yield the results intended by the Act. The state certification procedure fails to address the Tenth Circuit's mandate to induce states to remedy egregious discrepancies in intrastate rates. Lastly, the *RD* fails to appropriately address the needs of mid-sized ILECs which have been classified as "non-rural" for purposes of federal high-cost support, but which in fact are exponentially smaller than the huge BOCs with which they are included. In addressing the flaws in the *RD*, the FCC should not adopt the *RD* and should modify the current "non-rural" federal support mechanism as proposed herein, to make it consistent with the Act and appropriate for application to all carriers. In addition, the FCC should revise the definition of “non-rural” carrier to exclude carriers such as RTC.

Respectfully submitted,

SUREWEST COMMUNICATIONS

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